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AGENDA ITEM 6

TO: MEMBERS OF THE INVESTMENT POLICY SUBCOMMITTEE

- I. SUBJECT:** Policy Review and Consolidation Project – Proposed Real Estate Policies Project Strategy
- II. PROGRAM:** Real Estate
- III. RECOMMENDATION:** Information
- IV. ANALYSIS:**

Background

A comprehensive policy review was indicated as part of the Real Estate Strategic Plan recommended by the Board's real estate consultant, PCA Real Estate Advisors, Inc., and adopted by the Investment Committee in September 2007.

The Strategic Plan directed staff to review current assumptions concerning the portfolio in light of global investment conditions and determine where investment policies should be modified to reflect the new investment approach outlined in the Strategic Plan. Staff was also directed to bring revised policies to the Investment Committee, via the Policy Subcommittee, including establishing Value-Added and Opportunistic investment categories, as part of the Strategic Plan implementation timeline.

In addition to the Strategic Plan Implementation Item, existing Real Estate policies were previously scheduled for review as part of the overarching Investment Office Policy Review and Consolidation Project. This Project is a joint effort and includes input from the General Pension Consultant, the Board's Real Estate consultant, the CalPERS Legal Office, and the Office of Enterprise Compliance. The policies are being brought forward to the Investment Policy Subcommittee (Subcommittee) on a phased basis.

Proposed Framework

Staff has completed a review of existing policies per the parameters of the Real Estate Strategic Plan and the overarching Policy Review and Consolidation Project. Staff is recommending a single real estate policy. Staff believes a single policy will provide more effective policy directives and controls on investment activities. Please see Attachment 1 for a summary of review findings and proposed recommendations. Staff requests the Subcommittee's input regarding the following plan:

1. Aim to consolidate existing twenty-five (25) policies (Attachment 2) developed over time into a new overarching Real Estate Equity Policy that maintains all of the Board's directives and intent while reducing the number of current policies. New policy will mirror in form and structure, the policies of other private equity asset classes (i.e. AIM and ILAC).
2. Remove operational and procedural language from policies and place in Staff Internal Procedure Manual. Existing policies total 201 pages including extensive operational and procedural language. Removal of procedural detail from policies is a normal part of the Policy Review and Consolidation Project but may be more extensive for Real Estate compared to other asset classes due to the size in number and breadth of Real Estate policies. By moving procedural detail to the Staff Internal Procedure Manual, the policy will be more streamlined and clear.
3. Incorporate policy changes necessary to reflect new Strategic Plan and current global investment conditions. Major changes include risk categories, investment structures, benchmark adjustments, and leverage. Please reference Agenda Item 6 brought before the Subcommittee this month regarding proposed benchmark adjustments specifically.
4. Maintain Responsible Contractor Program, Accounting, and Appraisal and Valuation policies as stand alone documents. Conduct further analysis and consultation with the Legal Office regarding the incorporation of the Hazardous Material policy into the parent policy document.
5. The Fiscal Services Division and Investment Office Performance Monitoring Unit will propose and bring forward policy revision recommendations to the Subcommittee for the Accounting and Appraisal & Valuation policies separate from the Real Estate Unit's portion of the review process. The Real Estate Unit will no longer own these policies going forward.

Staff emphasizes that the proposed framework represents the creation of a new policy document that will be comprehensive in scope and incorporate changes

necessary to implement the Strategic Plan. Substantive changes from current policy will be reported with supporting rationale. However, given the extent of policy rewrite, policy submissions to go before the Subcommittee will not include black lined policies that have been part of the Investment Office Policy Review and Consolidation Project in the past.

PCA Real Estate Advisors, Inc., has reviewed and concurs with the proposed framework.

Implementation Timeline

The following timeline outlines the next steps staff proposes to undertake to begin implementation of the Policy Review and Consolidation Project:

Implementation Action	Expected Timing
Staff brings policy draft to PSC to begin Board review process.	October 2008 (1 st Reading)
Staff brings policy draft to PSC for additional review and comment.	December 2008 (2 nd Reading)
Staff brings proposed policy to Investment Committee upon approval of PSC.	February 2009

V. STRATEGIC PLAN:

The Real Estate Policy Review and Consolidation Project will further the following CalPERS Strategic Plan goals:

- Goal VIII. Manage the risk and volatility of assets and liabilities to ensure sufficient funds are available, first, to pay benefits and second, to minimize and stabilize contributions.
- Goal IX. Achieve long-term, sustainable, risk adjusted returns.

V. RESULTS/COSTS:

There are no material costs associated with this agenda item.

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